these questions, but I have been asking these questions now for the past few months. I have been asking a lot of lawyers and have not been getting any answers. The nice thing about economists is economists will actually tell you something and not worry about who it offends.

VOICE 1: Whether it is legal.

MR. FURCHTGOTT-ROTH: Right.

MR. ROGERSON: We will test this, Commissioner, if you would like.

MR. FURCHTGOTT-ROTH: Thank you.

MR. ROGERSON: Joe Farrell is dying to answer.

You know, I think you have raised very interesting questions, and I would love to spend five minutes turning the panel loose on it if it is all right with you.

MR. FURCHTGOTT-ROTH: Please.

MR. ROGERSON: Joe, go ahead.

MR. FARRELL: Okay. Thank you. To answer your questions, or try to, I think the issues are overlapping, and the standards should potentially be different. Let me try to explain that.

My understanding is the Commission is supposed to consider a fairly broad public interest test of whether mergers are a good thing or a bad thing. That is not necessarily the same question as DOJ/FTC are supposed to consider, which is whether they substantially reduce

competition.

I think the differences are in two areas. One is the FCC is trying to help along a process of increasing competition rather than just preventing it from being diminished, and that raises, of course, the whole issue of potential competition, how it is dealt with, what the evidentiary standards are in the Courts at the DOJ and FTC and whether those are the right standards for an industry where competition in some segments has been illegal until relatively recently and is still not going very far.

Then, of course, you will not be surprised to hear I think the benchmarking type issues, which I talked about this morning, are probably of more direct concern to the Commission than they would be to DOJ or other anti-trust agencies.

MR. FURCHTGOTT-ROTH: If I could just very quickly make a comment, Joe?

It is true that the Commission has some public interest obligations under 208 through 210 -- actually, we have public convenience and necessity under 214, but not a public interest obligation -- but those are for the transfer of licenses, not for mergers.

This agency handles over 10,000 license transfers every year, the vast, vast majority of which, more than 10,000 license transfers a year, which are never subjected

to any kind of public interest test.

We have no written rules about how we decide which license transfers are going to be subjected to a greater degree of scrutiny than some other license transfers. At least the Department of Justice has specific rules about which mergers it is going to review and by statute which will trigger a process and which do not.

We at the Commission do not have that sort of clear, written guidance. It is a little loose right now, I think.

MR. ROGERSON: You know, we are very fortunate to have two former chief economists from the Department of Justice with us today. I certainly would love to hear what both of them have to say about this.

Rich Gilbert, why do you not go first?

MR. GILBERT: The Department of Justice has guidelines for the review of mergers, but does not really have what I would call rules.

Each merger evaluation is a very fact specific exercise, and the ultimate question is in my view really a public interest test, although the analysis says first is there a threat to competition, is there a risk of harm to competition, and then if there is then do the benefits and efficiencies outweigh that risk of harm to competition.

I think the issues before the Commission should be

very similar. There may be some regulatory issues as well. In principle, you could actually say that that is also relevant to a DOJ analysis as well to the extent that the change in competition, if there is some, affects regulation, but I think that there should be a substantial convergence in the two standards, even if they may not be identically the same.

MR. ROGERSON: Bob Litan?

MR. LITAN: Actually, this was the very first thing that I was going to address in my presentation, and so I am going to carve it out from my presentation and preserve my time.

MR. ROGERSON: No, no. You are too quick for me.

MR. LITAN: Look, I had presumed that the FCC operated under a public interest standard because if it did not, there would be no role for the FCC. I mean, why even have the FCC rule on mergers?

My all around presumption is that is public interest, and I wrote down on my outline, which is out there for people to look at, at least three alternative tests that have never been made explicit, by the way.

In fact, in answer to your question, you are in the process or you can make case law in this area. I do not know the case law on the definition of public interest, but you can have three alternatives.

One is you could set the bar at a reasonable likelihood that the merger will just lessen competition, as opposed to substantially lessen competition, which is the Clayton 7 standard. That will be a slightly different standard that will be a little more strict than the DOJ standard.

You could then make it even tougher by saying that you had to find that the mergers may be pro-competitive, or you could go even further and try to find that the mergers are actually likely to be pro-competitive.

I think, frankly, when I discuss the outcome of potential competition analysis, the outcome depends heavily on which of these standards you actually apply, but I think you are in the process of writing the rules.

MR. ROGERSON: You know, I mis-spoke myself. I am betraying my great youth, I guess. A little middle aged joke there.

We have, I believe, a third former chief economist of DOJ in the room, which is, of course, Jeff Sheperd. I certainly want to hear from him as well.

MR. SHEPERD: I will be very brief. Collective memory is so short. In 1967-1968, I was the third of Don Turner's special economic assistants, so I am only half of the chief economist, but I was there when this all started, and I helped draft the guidelines on the mergers that he put

out in 1968.

I would only say in this matter that I think after some careful reflection that whatever anti-trust does is a help, but it should not set the parameters for what the Commission does.

MR. ROGERSON: I have asked all of the chiefs except one more chief economist, Michael Katz. Go ahead.

MR. KATZ: Actually, I want to address this problem from a slightly different angle, which people have been talking about should the standards be different between the Department of Justice and the Commission.

I think there is another difference because I think the standards should largely be the same. I think there is scope for some difference, but largely they should be the same. The analysis should largely be the same.

I think there is a big difference between the two agencies in terms of their ability to impose and to implement remedies. The Department of Justice rightly is loathe to get into regulatory solutions, and so when the Department of Justice evaluates -- you think it is not right, or you think they got into them?

MR. LITAN: We got into them all the time. I spent a year and a half negotiating them from deal to deal. That is what I did.

MR. KATZ: Fortunately, the people I deal with are

trying to stay out of them. In any case, it would not be right for them to try because they are not an expert agency.

I mean, there are some industries they obviously are involved in quite a bit, but their role is very different than that of the Commission and so I think that is what I see as I think the biggest difference is the sorts of remedies that are available and proper for the Commission are I think much more intrusive and expansive.

I know those are bad words these days in regulation, but I think the fact is that regulation is going to be around for awhile and I think that that is appropriate, although I share everybody's hopes that -- well, everybody hopes that regulation will go away. I think we differ on why, whether we hope there is also competition as the driver of it going away.

Let me also mention one other thing, and I know you are not supposed to be rude to your host, but I know a lot of things that I then do not listen to, and that is I think that the information that goes to the Commission is different than what goes to the DOJ because I think that unfortunately the Commission it is much more cumbersome to provide confidential information and for the Commission to act on it.

I do not know what the solution to that is, but I think it is something that I saw when I was chief economist

and I see now that I think does hinder the Commission's ability to analyze some of these things because these issues that we are discussing today, and Bob Crandall brought this up when people start asking about the business plans.

First off, we are the wrong set of people to ask about the details of it because we are not the business people, but also this is the wrong place to discuss it. These are very sensitive issues. It is sensitive for the merging parties. It is a sensitive issue for the parties that are concerned that they will be denied access, and that will force them to alter their plans.

I think, Commissioner, I am glad you are looking into this, and I think it is an excellent thing to do. I would add that to part of what you look at is how to deal with confidential information in a more streamlined or more effective way.

MR. ROGERSON: Okay. Now that we have heard from all of the chiefs --

MR. NOLL: Let me be an Indian. I just want to make the obvious comment. A group of economists is not the right group for Harold to ask the question simply because no matter how we slice it, we are always going to come down to the same set of criteria, right? We are trying to do things efficiently.

Both agencies offer in a political and legal

environment. That means the constraints, what they can do. Neither agency maximizes economic efficiency. All right. There are other constraints operating upon what they do from the legal environment in which they have been created and from the political environment in which they have to get their budgets and their staffing increase requests and all the rest.

Just the obvious point is the point about the way potential competition is taken into a place, the way the FCC worries about universal service, which is not a concern of the Department of Justice.

As economists, we have a hard time cognizing exactly how we are going to take into account these constraints, but it seems to me the real reason why the FCC has a separate and independent authority to review mergers is in fact a public interest issue that in part goes beyond the economic efficiency criteria.

It means two things. It means that we as economists are not going to write all the rules, but, secondly, it means that within the domain of efficiency maximization there are going to be actions and strategies and decision rules available to the FCC that are not available to Justice and vice versa, and so I think part of what should be going on here is taking into account the feasible set of policies and rules, as opposed to the best

of all possible worlds set, which I agree are largely the same in the two environments.

MR. ROGERSON: Bob Crandall?

MR. CRANDALL: One brief point that is kind of ironic. Rich talked about enforcing the Clayton Act at Justice.

In fact, fortunately, Justice does take into account efficiency gains from a merger for two reasons. One is to balance it against any potential cost, and, secondly, it wants to see if this is really the reason why firms are merging or might it be an attempt to monopolize.

In fact, under the Act such a balancing is not permitted. The Act says any lessening of competition that tends to create a monopoly in any line of commerce has to be stopped. That means you do not bring some cases you could win.

When Jeff worked for Don Turner, Don Turner was accused of treating the Supreme Court like a bunch of C students in his course, but the irony here is that you can take benefits into account, whereas formally in a Court of law it is more difficult for Justice to do it.

To the extent that you can take them into account, it is hard to imagine benefits being negative. This would suggest that you are more likely to approve a merger than DOJ is.

MR. ROGERSON: Dennis?

MR. CARLTON: I will be very, very brief. I have never been a chief economist at the Department of Justice, although I worked there a little bit. If I did fractions, I would be below a half. I did help write the recent merger guidelines, though, so maybe I am epsilon above zero.

I guess I agree with a lot of what Michael Katz said. I think I disagree a bit with what Joe Farrell said and Bob Litan. I think it would be a mistake if the FCC adopted different standards for potential competition or for benchmarking.

The Department of Justice should be concerned if a merger will cause a harm in an industry by impairing regulators and that will adversely affect competition. That strikes me as something that should be taken into account.

I am glad I am seeing someone from the Department of Justice shaking their head and agreeing. I think that the standard that the Department of Justice uses in evaluating mergers is the correct one. Exactly how the Courts interpret it or not, I think the way it has been implemented, how the Courts would interpret it, the way it has been implemented at the Department of Justice, my understanding is, they do take account of total benefits and total cost.

I think it would be a mistake to have a different

standard at the FCC. However, I think there may be special categories of customers, such as those you want to protect through universal service, that raise special issues that the Department of Justice would find outside their realm of expertise and may not pay attention to. That is something the FCC should be concerned with.

I do not see that arising in any of our discussions this morning, but if there were such a group of individuals that the FCC is charged with making sure they are protected in some way, that would be a special difference.

The other difference is you have special expertise that gives you the ability perhaps to analyze things either differently, not with a different goal, but just to come to different conclusions because of your past experience or, as Michael said, the reluctance to impose regulatory solutions, complicated regulatory solutions. They may not seem so complicated to you guys as to the Department of Justice.

I think those are the differences, but in terms of fundamental goals under anti-trust, the standards I think should really be the same.

MR. ROGERSON: Rob, I have to call on you.

MR. GERTNER: Just to complete the picture.

MR. ROGERSON: Right.

MR. GERTNER: I think that I basically agree with

what Dennis just said.

When you think about the public interest standard, you know, the guidelines and the way the Justice Department analyzes mergers has seemed to be and have turned out to be a very effective way I think of promoting the public interest in merger analysis, the notion that, you know, absent evidence of substantial anti-competitive harm, we want to allow mergers to go through.

That is a standard that works well because in fact it does promote the public interest in general, so I think that by and large I agree with what Dennis said.

MR. ROGERSON: Commissioner, would you like to raise any final issues?

MR. FURCHTGOTT-ROTH: I thank all of you for your comments. They are all very thoughtful. I have learned a lot and will try to take those into account as we move forward in reviewing these. I am glad you are here on a telecom matter. We are not here on Exxon Mobil or Amoco BP.

I still have a lot of questions and look forward to reviewing the entire session. Thank you very much.

(Applause.)

MR. ROGERSON: All that repressed, you have only 30 seconds I am going to take out on Bob Litan now.

So now back to business. No more running on. We are going to turn to the issue of effects of actual and

potential competition of this merger. Bob Litan is going to begin, then Jeff Sheperd will make remarks, and finally Rich Gilbert will make remarks, and then we will turn it loose.

Go ahead.

MR. LITAN: Okay. Just one last word on the standard because it is a lead in to my discussion. The question is should the standard of the FCC be that you have to have a winnable Clayton 7 case in order to stop a merger on competitive grounds, or should you be able to stop a merger on something short of a Clayton 7 standard?

All I am going to say is that my analysis or the outcome of the analysis rests heavily on which of those two things you believe. All right.

Now, on actual competition my belief is, subject to being corrected, that there is very little actual competition between any of these parties except perhaps in some regions in wireless. Where that is true and where that is a potential problem it is easily fixed with divestitures, so I do not think it is a big deal.

The only thing that I think is interesting here is potential competition. Now, the Justice Department, to my knowledge, has never won a case on potential competition. On the other hand, they have never had a monopoly situation where potential competition should matter more. You should care more about the presence of contestability where you

have a monopoly to begin with.

Therefore, you want to look at the number of potential entrants that are out there before the merger, after the merger and whether the merging parties, any of them, are the most likely successful potential entrants. Those are the things you want to look at.

What I did in my piece is I prepared a little chart for the three different markets, telephones, TV and advanced services, and I tried to tabulate who were the potential competitors there.

The bottom line of that complicated chart is this. I had assumed that except for the merging parties that there are no other RBOCs that are likely potential entrants in these markets. I do not believe that they are significantly likely entrants, so you have one other potential RBOC plus three main long distance companies is what it comes down to in telephones.

I know you have the CLECs. I know the arguments about electricity and cable and all that. I view all that down the road, and the CLECs are minnows. All right.

So really in the telephone market you are talking about going from basically four to three is what it comes down to. Would that be a Justice Department case? No. I do not think Justice could win on that. Could it be a case here? That is an open question. It depends on what your

standard is.

The second market, TV. There you have fewer potential competitors. My argument there is you have AT&T. They are marrying with TCI and Time Warner. It is not clear how any other long distance guys are doing it.

We have wireless companies' satellites already in this, but they are inhibited because they cannot show local broadcast, although the FCC could change that rule and make them into real competitors, which, frankly, they should. A side commercial.

In any event, in the absence of that, there are fewer potential competitors in TV, and there appears to be some evidence Ameritech is already in TV in its local area. I have not seen the corporate documents, but if there are corporate documents that show that Ameritech was planning to get into TV outside a region, that could be more significant. All I am telling you is there are fewer potential competitors in TV. There is more likely to be a problem under any standard you look at.

Finally, in advanced services it is anybody's guess. I have basically a lot of unknowns, a lot of questions, and I am really not going to make much of a call in that area.

The final point I will raise is that if you believe there is a problem, conditions can fix problems.

One condition that the FCC could seriously consider is what they did in Bell Atlantic-Ninex. Remember, they originally had their unbundling rule, their uni unbundling rule. It was challenged in the Courts. We all know what happened eventually in the Supreme Court, but the FCC went ahead despite the challenge and imposed its original rule in Bell Atlantic-Ninex.

So what the FCC could do now in the wake of the Supreme Court decision, which, as I understand it, basically said that it was okay for the FCC to have a rule on one uni platform, but on multiple uni platforms they had to go back and do their homework, so theoretically the FCC could just go ahead and impose their original multi multiple uni platform rule as a condition for both mergers.

Open question though as to how much additional pro-competitive effect you get relative to offering just one uni platform. I do not know what the answer to that is, but all I know is that if I was the FCC, I would be seriously considering adding that as a condition if I was going to go ahead and approve the mergers.

MR. ROGERSON: I have now got to tell you you only have 30 seconds left.

MR. LITAN: I talk fast.

MR. ROGERSON: What I would like to do is give you 30 seconds to tell us what a multi uni platform versus a

single uni platform is.

MR. LITAN: Well, this opinion was a mess, as far as I was concerned. The way I interpret it is the Supreme Court said that the Bells had to offer at least one platform or one combination of unbundled network elements at essentially incremental costs, long run incremental costs, but that the Supreme Court questioned.

That is the way I read the opinion, and I could be wrong. It questioned whether or not the FCC could force the RBOCs to offer multiple platforms so that other people could pick and choose in effect which pieces they wanted and that the FCC had to go back and do its homework.

Now, I could be wrong about that interpretation, but I am still quite confused about what the Supreme Court said. I may not be the only person in the room about that. A lot of people were confused.

MR. ROGERSON: Thanks, Bob.

Jeff?

MR. SHEPERD: Thank you. I am here as an economics colleague of people at the table and some of you. I have an outline of two pages of my main points. The copies are probably gone, but I could try to give it to you if you asked me later.

In general, I do not think regulation is so bad. The compulsion to get rid of it should not be so strong. I

do not think anti-trust is so good, particularly on mergers. I am not impressed with the concepts that are cobbled together in the merger guidelines now, and I think the division on the whole has weak enforcement of those rules. I think the research basis about mergers, both in business and economic research, is that most of them do not work out even for their shareholders, as well as for the public.

Earlier I said that this is a difficult and an unstable period in which managers of telecom firms may well feel compelled to merge in a self-protective way. Solving this arms race is a major problem for the FCC.

In fact, I think of this merger, both of them in fact, as trial balloons. They sent them up thinking well, let's try it and see if it works. We do not really expect them to sail through, but the other feature perhaps is that these mergers would tend to nullify the basis the FCC put forth for approving the Bell Atlantic-Ninex merger. That is, they counted on conditions which now would no longer be true if these mergers go through.

However, rather than focus on these two mergers, I would like to just remind us of basic economic points that are relevant. First, this is not just a matter of static efficiency. Society wishes for innovation and other good things from mergers, not just a narrow price equals margin of cost consumer surplus maximizing result.

Second, effective competition requires three main things. One, you need five, or maybe more or maybe one less, actual comparable competitors, not just two or three. If you want a horse race, you have to have horses.

Also, dominance tends to suppress or distort competition, and also you need easy entry, so the basic target and the basis, I suppose, on which 271 might be decided is are there enough competitors so that they will not collude? Is there dominance, which does not permit effective competition, and is entry really easy?

I would stress dominance really matters. It is not just a neutral condition, and deregulation has tended and does tend to get detoured into a dominance trap. The monopolist learns to live with ten, 15, maybe 20 percent of the market as competitors, but then says no and from then on expects to live with most of the market. In fact, that is my reading of the business press. The Baby Bells expect to keep 80 percent of the market right on into the future.

I do not think that is good enough for the FCC or for anti-trust, for that matter, and in the process towards effective competition mergers are the main danger. They are the thing by which companies can directly stop the progress toward effective competition.

Now, whether these mergers are that way is open to debate. Everything among economists is a two sided issue.

There is a balance to be struck, and it may tend one side or the other. Of course, we can differ on these, but to say everything is all one way or the other is lawyer talk, not economics talk.

As for barriers, there are many sources of barriers. I usually discuss 18 or 20 of them. It is not a matter of just --

MR. ROGERSON: In 30 seconds, though.

MR. SHEPERD: -- a few. I will be very quick. Among them are not just the exogenous conditions of size and money needed to enter and so forth, but endogenous strategies and tactics that companies can play to defeat entrants.

In general, the burden of proof should lie very strongly against self-interested claims about the balance of the goods and the bads, and that is very important for the FCC that it not just treat everything as kind of everybody has the same amount of credibility.

Finally, any gains must be net; not just something you can show, but it would have to be strictly net. Now, finally in my outline I go through the reasons why competition would on balance, I think, be hurt by these mergers, but that is what I was hoping to gather, the data on these things, not just announcements of positions.

MR. ROGERSON: Rich Gilbert?

MR. GILBERT: There is no potential competition case here period. Now, I still have five minutes, right?

MR. ROGERSON: Well, four and 50 about.

MR. GILBERT: Okay. Let me show a list of the existing competitors in St. Louis. You are not going to be able to read from this, so I will read from it.

Facilities based. MCI WorldCom is in St. Louis, and this is one of the key issues, I think, on a potential competition analysis. Are we talking about possibility of Ameritech moving into St. Louis? AT&T through TCG Teleport, Intermedia, Digital Teleport, Frontier, Birch Telecom, Winstar, Sprint has announced its Ion entry, Telegent has announced that it will enter, and we have AT&T-TCI, resellers. There are a couple of resellers as well. The list that I mentioned is facilities based.

If you look into Chicago, that issue has been raised. The list is probably twice as long in Chicago. If we are talking about what I call conventional CLEC style entry, which for an RBOC or any ILEC would mean somebody going out of region, setting up as a standard CLEC, there are lots of folks who can do that. There are a lot of folks who have been doing that. If that is the issue, there simply is not a potential competition case here.

What do you have to show for potential competition? You have to show that you have a firm that is

a likely potential entrant. You have to be able to say that someone actually is going to enter, as opposed to well, maybe somehow somewhere someone could enter. If that is the standard, everybody is a potential entrant.

You have to show that if entry occurred, there would be a substantial deconcentrating effect, which translates into an effect on prices and the market, and you have to show that the potential entrant is one of a few because if there were many potential entrants, then taking one of them out really does not do anything.

The issues that have been raised in terms of what types of potential entry would be eliminated -- could be eliminated -- in this transaction are Ameritech's entry into St. Louis and a possibility of SBC into Chicago.

I mentioned before the issue about SBC in Chicago was under the old plan of a possible wireless platform based entry. SBC tried that in Rochester. It was very unsuccessful. They abandoned it and decided that that is just not a good way to go.

Ameritech into St. Louis. The history, the documents show, and I think these are public documents. I want anyone to stop me if I am divulging confidential information. The documents show that there was a contemplation of offering resold SBC local service.

It would be advertised -- this is SBC local

service, along with Ameritech's wireless service in St. Louis -- as a defensive measure because Ameritech was concerned that they were going to lose wireless customers to other wireless providers, PCS and cellular providers, who were about to provide bundled services.

There was an experimental entry. It had not happened. The merger came along. It is off the table. Any contemplation of entry in St. Louis is as a reseller to the extent that there is any entry at all. There are plenty of people who can do resale.

There was no intention of doing any facilities based entry, and it was not an attempt to get into the local exchange business. It was an attempt to protect the wireless customers. For that matter, if these assets are divested as they would have to be --

MR. ROGERSON: Rich, I was so swept away by this. You only have 20 seconds left.

MR. GILBERT: All right. I got carried away too.

Someone else can take over these assets and do the same thing. The bottom line, and I am going to finish, there is not a potential entry issue in this merger.

MR. ROGERSON: Robert Crandall, is that vertical name plate meant to be?

MR. GILBERT: I am talking, by the way, about SBC-Ameritech obviously.

MR. CRANDALL: I think the reason why the Courts have been reluctant to accept potential competition arguments is they are, of course, speculative. The notion that even though the Commission is a specialized Commission with expertise in telecommunications, the notion that any of us in this room today can predict how competition is going to unfold in this industry is, it seems to me, presumptuous.

I think those who are in the process of writing opinions, which unfortunately will not disappear in the next few years and will have to be revisited, might be in an embarrassing position if they tell us that the list of potential competitors is limited only, as Bob said, to four or five.

The last time around in Bell Atlantic-Ninex, we were told that the potential competitors were only the two relevant ILECs plus the three interexchange companies. Cable companies were excluded, yet since that time it turns out that AT&T, in order to compete apparently, has to have the largest cable company in the country and sign up agreements with other cable companies. It seems to me that tells us that the cable companies, at least by AT&T's admission, and they may be wrong again, are in the market for potential competition.

It may also be true that other media; for instance, I brought this along not because I plan to annoy

you and use it in the room today while we are talking, but I bought this service when the cost had fallen to ten cents a minute. Since I bought it three months ago or two months ago, the cost of my service has fallen to 8.3 cents a minute.

By the time this case is on appeal, if somehow these mergers are reversed, I will be perfectly willing to explain to you why it is that I have torn out my copper wires at home because the futures price of copper has gone up a bit, and I just melted it down, and I am using this alone.

It seems to me that we are getting to the point where the bottleneck is contestable from wireless at a rapidly accelerating rate. It does not have to be Project Angel. It does not have to be any other fixed wireless companies. It just is this little handset, which I can buy for $100 and can change my service on a moment's notice.

I think it is a very dangerous proposition to try to limit the number of potential competitors and base on opinion on that. Even if it gets through the Courts, you are going to be embarrassed by it in the future.

MR. ROGERSON: Joseph Farrell?

MR. FARRELL: Thanks.

Well, actually I agree with quite a lot of what Bob Crandall just said; not all of it. I think it is

obviously true in this industry that predicting the course of competition is pretty tough, and I think the question that that should lead to is what should you do about the fact that there is so much uncertainty?

It seems to me one almost immediate reaction that an economist should have is you want to behave in such a way as to sustain the existence of as many options as possible, and it seems to me that does have an implication for what we are talking about here because it is likely to be much easier to allow these mergers after a year or two if it turns out that wireless really does bypass the local bottleneck than it would be to undo them if the opposite state of the world turned out to be true and if it turned out that there were bad consequences from the mergers conditional on the continuing local bottleneck.

I would also like to just offer one comment on the way that people list potential competitors and treat the number of entries in the list as the relevant thing. That is not really quite right. What we should be looking at is whether there is a substantial probability that the merging party who is not currently in the market would turn out to make a big difference to the state of competition in the market.

You could have an adjacent ILEC who is a potential competitor and 963 other potential entrants, but a situation

in which the entry probabilities are not all that well correlated, and still have a substantial probability that the adjacent ILEC would make a big difference to the state of competition.

I do not know enough to say that that is the case, but if you think that, for example, the argument that other ILECs, perhaps particularly adjacent ILECs, have particular expertise in negotiating interconnection or have particular forms of brand image or something, if those arguments are at all plausible then pari passu the argument is plausible that this precluded potential entrant would make a big difference.

It does not matter how many other potential entrants there are who would be a competitive force in the other state of the world where those particular assets turn out not to be the key thing. I think I agree with Bob. We cannot really predict very well which of those states of the world is the case, so I think we need to think about how to make decisions, taking into account the uncertainty.

It is unfortunate, I think, that the Commission seems to believe it is required -- whether it is or not, I do not know -- to write its decisions in a way that suggests we understand everything, and we know that this is the right decision.

I think it would be a lot better in many cases,

and this may be one of them, if the Commission were more comfortable with saying there is an awful lot we do not know. This seems like the prudent thing to do at this point, given that fact.

MR. ROGERSON: Okay. I thought that was a good question. Joe said he is not sure that the ILECs are necessarily the only potential significant competitors, but it could turn out that way and so why do we not wait a few years and see at a minimum, right? Go ahead.

MR. FARRELL: Wait and see also whether the existing local bottleneck continues to be a local bottleneck.

MR. ROGERSON: Yes.

MR. FARRELL: That is also relevant.

MR. ROGERSON: Okay.

MR. GERTNER: I think that that would be the wrong way to look at it. I think the reason why the Justice Department is wary about using potential competition is because when you are uncertain about the effects that whether or not the potential entrant will actually come in, then you tend towards allowing markets to operate.

Now Joe wants to add another layer of uncertainty here, which is the layer we do not really know what characteristics of potential competitors are actually going to be the relevant ones that are going to determine who is

going to be successful competing in these markets. Therefore, what we are going to do is we are not going to allow companies to do what they think in fact is in their interest and, therefore, most likely absent tangible anti-competitive effects to be in consumers' interests as well to go forward.

I think if you look at it, you have to say what is it that are the unique characteristics of the merging parties that give them some potential benefits I think when you go down that list. The fact that they are an ILEC; well, there are lots of other ILECs, and in fact others trying to enter this market are doing it by buying CLECs rather than buying ILECs, so that does not seem to be it.

Is it proximity? Well, there are lots of companies that are nearby, lots of other competitors nearby. Why does proximity matter anyway? You say maybe it has to do something with brand name. You have to ask how important is that, given that they are not actually serving the customers. In fact, it is knowledge or having existing customers that is most likely to be the source of an advantage.

I think when you look at it and you try to identify the unique characteristics of merging parties outside of their region, there really are not any that would make you conclude that it is likely that they have some

unique position to have an impact.

MR. ROGERSON: Okay. I want to pursue this just for one more minute. I think Rob has said it is not very likely at all that ILECs are likely to be one of a small number of significant potential competitors. He cannot think of too many things that they have that are likely to really matter.

Could I give Joe a chance to respond to that?

MR. FARRELL: Well, I would come back to my confidence statement that we do not know. I think, you know, the statements that have been made from both sides of this debate that large ILECs can be more efficient in various ways than small ILECs have some implications for whether little CLECs are going to be a full replacement for the kinds of things that a large ILEC might decide to do in some national/local strategy.

I think Dennis has harped on -- let me take that back. Dennis has stressed a view of the national/local strategy that says there is no evidence that the firms would undertake it individually, and then he has given some arguments why that might be less plausible, but I think the bottom line from that is not we should assume it will not happen, but we do not know whether it will happen.

Again, I think, you know, I have not looked into this particular question deeply, so I cannot really give you

a bottom line, but I think the right thing to do is to investigate with a very strong consciousness of how much is unknown not whether it is more plausible or not or not whether it is convincing or whether we should assume, but whether there is a sufficiently big chance that it would be imprudent to ignore that any particular potential entrant will turn out to be important.

I think that is the right way to frame the question. I do not know what the answer is, but I think that is what the staff and the Commission and, for that matter, the Department of Justice probably should be doing.

MR. ROGERSON: Okay. My neck is getting sore turning this way, so I am going to now turn to Robert Litan for a moment, who has been patiently waiting over here for his turn.

MR. LITAN: Yes. Thank you.

You do not know whether an ILEC is likely to enter until you look at the documents, all right, at least when we are looking at adjacent ILECs because I do agree that if you are not adjacent I do not see any evidence at all from the last two years that non-adjacent ILECs are interested in entering.

We come down to documents. We know in the case of Ameritech there was documented interest in crossing boundaries and going into SBC's territory. We know that. I

do not know the record in Bell Atlantic-GTE as well, but at least on the surface it seems to me they have less of a problem than certainly Ameritech would because GTE is dispersed all over the country, and it seems to me less likely that Bell Atlantic would be interested in going into little pieces of GTE's territory. In any event, this comes down to documents. That is point one.

Point two is in a way that is all irrelevant because I do agree with Rich that if you count the three big interexchange carriers, you have that plus the adjacent RBOC. You have four already, and that is going to at least eliminate any Clayton 7 standard right there, a Clayton 7 challenge, and it is going to be hard to make the argument that the FCC but for one fact, which is the third point.

That is we talked about it earlier. What happens when we get down to one RBOC, all right, or one ILEC? I mean, the thing that still would trouble me very much if I were sitting at the FCC is these mergers go through. What rationale would the FCC then use to stop the next mergers?

If there is no such rationale, then why not go the limit and go all the way to one? If that is where we are going, then it seems to me Joe was asking exactly the right question, that knowing that it is legitimate, it seems to me, for the FCC to take into account the uncertainty about all this, and you really then have to believe that there is

a very strong likelihood of a pro-competitive effect.

You have to believe Dennis' story that they are going to go into 30 other cities in order for you to overcome this nervousness you have about collapsing to one ILEC. I mean, I have been persuaded that that is the case, but if I were in the Commission that is the balance that I would have on my head because the end game here, it seems to me, cannot be ignored.

MR. ROGERSON: I am going to Dennis Carlton and then to Roger and then to Rich.

MR. CARLTON: I have three quick points. The doctrine of potential competition has fared poorly because it is very hard to predict the future. To give up certain benefits for something that might occur in the future just turns out to be very difficult.

Now, I would like you to especially recognize that in a rapidly changing industry predicting who is going to even be the leader in that industry is not so easy, let alone who is going to be the participants.

I once had occasion to work on a merger that was unsuccessfully stopped in part on the grounds that the two companies would engage in new innovations and compete harder against each other than if they were merged. That was five or six years ago, and I am still waiting for those new innovations to occur. I will not embarrass the person at

the Department of Justice at the time who I told this to.

When you go through rapidly changing industries and try and predict, just go through five years ago and look at the list of people who are in telecommunications today and ask yourself would you have predicted some of these names? I think the answer is it is pretty speculative. It is pretty hard.

Second, I think it is easy to say let's be careful. Let's wait. That sounds like you are being careful, and there is no cause. You have to recognize that by being careful and waiting, what you are really doing is making life easy for a regulator. You are not making life good for consumers.

My interest is in making life good for consumers, which may require regulators to make difficult decisions. It is an easy decision to say wait, let's see in the future. What you are depriving consumers of, though, in the meantime could be significant, very significant, benefit.

Finally, to get to Bob's question about one, I think the answer is one. I believe what these companies are saying. These two companies that are merging are going to be horizontal competitors. I would say no to that. I mean, I do not know. It may get me in trouble in the future. They may not hire me, but that is life, you know. One is too few. They are horizontal competitors right now.

MR. NOLL: The lawyers did not read that one.

MR. ROGERSON: Roger Noll?

MR. NOLL: I actually just want to ask some questions because it seems to me that by revealed preference we know that Ameritech wants to be in St. Louis and Southwest Bell wants to be in Chicago, or they would not be proposing to merge.

Number one, if that is true then each one wants to merge in the profit maximizing way, wants to enter in the profit maximizing way. Combining and having roughly 80 percent of the customers be monopolized is going to be better for them than going in and sharing those 80 percent in two 40 percent hubs, assuming that were feasible.

So, it seems to me that we know that they want to be in other territories by virtue of the fact everybody wants to merge with everybody. Secondly, we know that by far from the company point of view, the most attractive way to be in other places is to actually acquire someone who is there.

The absence of direct entry by RBOCs into other RBOCs' turf strikes me as fairly understandable from our normal strategic theories that they think that it is very possible that in the long run they will be able to go to the two or three ubiquitous ILECs, each of which in its own service area has 80 percent of the market, and that as long

as that strategic possibility is available they do not want to do anything that makes it less likely to happen.

If the FCC were to say for certain we are done with large ILEC mergers, there will never be another one as long as we live, then conceivably Ameritech's attitude about acquiring one of the 973 CLECs in St. Louis, that that calculus would change.

In particular, the question that I have is if there is this natural efficiency advantage of a large ILEC providing service in St. Louis by merging with Southwest Bell, say Ameritech, why is there not also the same efficiency advantage for them buying one of these 973 guys who are already there and having the integration, the technical sophistication and the original advantages that the proponents of the merger say apply to a much littler company where they might in fact be substantially greater?

It strikes me that what is really the reason that Ameritech does not want to acquire one of these little, tiny guys in all the big cities in Southwest Bell turf is not because of some relative efficiency advantage. It is because they would prefer to have a monopoly position throughout both territories than to be a competitor, a large, significant competitor in those territories. They are not going to do the competitive strategy unless the monopoly strategy is foreclosed.

MR. ROGERSON: Rich Gilbert?

MR. GILBERT: Saying no is not without cost. What are the costs? The costs are that you give up the range of services that could be provided under this national/local strategy that SBC-Ameritech have and a version of that that Bell Atlantic has as well, so you give up those benefits.

Also, there are other costs as well, which is you do not have a good horse race when you let three horses out of the gate first and then you tell the rest of the pack to wait and see what happens. It would be best to have competition and end to end services occur simultaneously with everybody throwing as much at it as they can.

Now, it is important in my view, very important, to distinguish what I call conventional CLEC style entry from the national/local strategy. I think this is a key issue in the merger. If you look at conventional CLEC style entry, that just means somebody goes into an area, tries to capture some profitable customers, may put in a switch, may put in a few switches. There are lots of folks that can do that.

There is no evidence that I see that adjacency is particularly important for that because none of the RBOCs have ever said that they would go into these adjacent territories because they have excess capacity in their networks and they are adjacent networks and they have,

therefore, low costs, incremental costs of going into new areas.

The fact is they do not. If they went in, they would either go in as resellers, or they would go in with new facilities and usually without much brand name recognition in any case.

What you really have to contrast here is the benefits of a national/local strategy type entry against what are probably insignificant issues in terms of conventional CLEC opportunities without the merger. That would be just essentially no effect on the conventional CLEC competition that would occur without this merger.

MR. ROGERSON: I am going to take two short comments from Michael Katz and Rob Gertner, and then we will take a couple questions from the audience.

MR. KATZ: I agree with people who are saying that potential competition analysis is difficult. There were two points they were making about that. One, that plans can change. It is impossible to predict the plans of even a single carrier.

The other is that there in fact could end up being a lot of rivals in the future. The only point I want to make here is it seems to me that that applies then with equal force to the earlier arguments we heard this morning about the benefits of the national/local strategies and the

expansion.

Even if we take it as given that the mergers are necessary and sufficient to get that expansion, it seems to me the arguments being raised here then have to be raised there as well of wait a minute, is it not possible there are going to be all sorts of rivals coming in so in fact that these parties are just a little blip on the radar screen of no real significance and so we should not give very much weight at all to the fact that they will be able to do this? It seems to me that is just a mirror image of saying taking them out, even if it were true, would not matter.

I am not saying that I have analyzed that issue. As I said, I agree that potential competition analysis is difficult, but it means we have to do the full analysis, and those questions have to be addressed.

MR. ROGERSON: Rob?

MR. GERTNER: I just wanted to make a quick comment about some aspects that are specific to the Bell Atlantic-GTE merger.

It is important to remember it is not just an ILEC buying an ILEC, but in fact a large part of the benefits from the merger come from the complementary assets of GTE's GNI fiber optic network and their Internet backbone, which is an important part of their entering into local markets.

To some extent responding to what Roger Noll said,